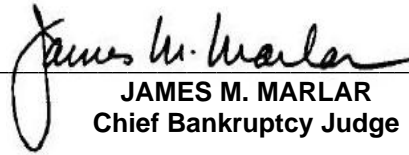


SIGNED.



Dated: October 27, 2009


JAMES M. MARLAR
Chief Bankruptcy Judge

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

In re:	)	Chapter 11
AVC VILLA DEL LAGO AT OCOTILLO	)	Case No. 2:08-bk-06834-JMM
DEVCO, L.L.C., an Arizona limited liability	)	(Jointly Administered With
company, fka AVC SWEETWATER VILLAGE,	)	No. 2:08-bk-06836 and
L.L.C., dba VILLA DEL LAGO,	)	No. 2:08-bk-06837)
Debtor.)	
MEMORANDUM DECISION		
In re:	)	(Re: Motion to Alter/Amend
AVC ESTRELLA VILLAGE DEVCO, L.L.C., an	)	Judgment by Arizona Village
Arizona limited liability company, dba THE	)	Operating Company, Inc., and AVC
VILLAS AT MOUNTAIN RANCH,	)	Service Company, LLC)
Debtor.)	
In re:	)	(This Filing Applies Only To Villas At
THE VILLAS AT OCOTILLO, L.L.C., an Arizona	)	Ocotillo, L.L.C., Case 2:08-bk-06837)
limited liability company, fka FOX VILLAGE)	
VILLAS AT OCOTILLO, L.L.C.,)	
Debtor.)	

On September 22, 2009, this court heard oral argument on a motion to alter/amend the confirmation order filed by The Arizona Village Communities Operating Company, Inc. ("AVC") and AVC Service Company, LLC (previously known as Desert Fox Associates) ("Desert Fox") (DN 50, 08-6837). The confirmation order was entered for The Villas at Ocotillo case ("TVAO") on August 12, 2009 (DN 201, 08-06834). This motion was timely filed within ten days thereafter.

1 After argument, the court allowed additional time to the parties to further brief issues which were
2 raised at the hearing. The parties have now done so, and the court feels adequately prepared to rule
3 on the issues.

4 5 **ABOUT THE DOCKET** 6

7 The names of the three Debtors and their affiliates are confusing throughout. It takes
8 a steep learning curve to figure out who the parties are, and how they are related to one another. In
9 doing its preparatory work for this Memorandum Decision, the court noted that many pleadings
10 were cross-docketed across the three files, and that items may be (for example) filed under one case
11 number but be related entirely to another of the three cases. Any reviewing party or court should
12 be aware to cross-check all three Debtor files, in order to grasp the complete picture of the three
13 Debtors and their affiliates, officers and owners.

14 15 **INTRODUCTION** 16

17 What might appear, on the surface, to be a rather routine matter, is not. The issues
18 raised by the moving parties are complex, and legally and procedurally deeply-rooted in bankruptcy
19 jurisprudence.

20 Whether a person or entity is affected by a confirmed Chapter 11 plan, and is bound
21 by its terms, requires an exploration, from many facets, of how the law works on a legal and
22 practical level, what the relationships are between the interested parties, how deep and interwoven
23 those relationships are, and whether the parties received adequate notice in order to present or
24 protect their positions in a timely manner.

BACKGROUND

A. Pre-Bankruptcy

Before bankruptcy, the three related Debtors were engaged in an integrated business relationship to acquire, build, finance, develop and manage residential real estate. The individuals behind the entities were Richard C. Harkins and Susan Harkins, and Richard H. Heesch and Rea Heesch.

In the course of such enterprise, several legal entities were formed, each of which had a direct or indirect role in the collective enterprise. In some instances, other unrelated corporations became associated with the Debtors' entities or individuals in the business ventures. One of those unrelated third parties was Kitchell Custom Builders, LLC ("KCB"). KCB's role became dual in nature, acting as both the building contractor and a minority member of a management entity.

Eventually, the real estate developments failed for lack of funding, and each of the Debtors' related entities filed for Chapter 11 on June 10, 2008. At this time, then, blame began to be asserted.

B. Chapter 11

Three related voluntary Chapter 11 cases were filed on June 10, 2008. They were:

Name	Case No.	Outcome
AVC Villa Del Lago at Ocotillo Devco, LLC ("Lago")	2:08-bk-06834	Dismissed per minute entry dated 08/12/09 (DN 202, 08-6834)
AVC Estrella Village Devco, LLC ("Estrella")	2:08-bk-06836	Dismissed per minute entry dated 08/12/09 (DN 202, 08-6834)
The Villas at Ocotillo, LLC ("TVAO")	2:08-bk-06837	Creditor's plan confirmed on 08/12/2009 (DN 201, 08-6834)

1 Although the three cases were jointly administered, only one, TVAO, proceeded completely to a
2 confirmed plan of reorganization. The remaining two were eventually dismissed.

3 The June 10, 2008 petitions in each case were signed by Richard C. Harkins, as
4 President Member and/or Manager of each of the Debtors, and of each of the entities which made
5 up the membership interests in the three Debtors. And, in each instance, one of the moving parties
6 here, AVC, was one of the entities involved in each Debtor. In each case, AVC assisted in payment
7 of the attorneys for the filing of the cases. *See*:

8

Lago	Case 08-6834	DN 14	para. 7-8
Estrella	Case 08-6836	DN 10	para. 7-8
TVAO	Case 08-6837	DN 15	para. 7-8

11

12 Moreover, AVC was listed on the master mailing list in each case, which lists were signed by
13 Richard C. Harkins, as the responsible member of each entity. *See*,

14

Lago	Case 08-6834	DN 7
Estrella	Case 08-6836	DN 5
TVAO	Case 08-6837	DN 5

17

18 Richard C. Harkins signed each of the statements concerning each mailing list, on behalf of AVC.

19 The three Debtor's addresses, in each petition, were the same:

20

Lago	Case 08-6834	1777 W. Ocotillo, Ste 15, Chandler, AZ 85248	DN 1
Estrella	Case 08-6836	Same	DN 1
TVAO	Case 08-6837	Same	DN 1

24

25 This address is the same as AVC, which signed (through Richard C. Harkins) each of the petitions.
26 *See* master mailing lists:

27

Lago	Case 08-6834	DN 7
------	--------------	------

28

Estrella	Case 08-6836	DN 5
TVAO	Case 08-6837	DN 5

Turning to the schedules and statement of affairs for each Debtor entity, the following other facts appear:

Lago; Case 08-6834

DN 23 - Schedules

Schedule F - Unsecured Creditors	Desert Fox Associates \$115,000 ¹
Schedule H - Co-Debtors	<ul style="list-style-type: none"> • Arizona Village Communities Operating Company ("AVC") • Richard and Susan Harkins • Richard and Rea Heesch

DN 24 - Statement of Financial Affairs

No. 3 - Payments to Creditors Within Prior Year	Desert Fox Associates - Numerous payments
No. 19 - Locations of Books, Records and Financial Statements	Arizona Village Communities Operating Company, 1777 W. Ocotillo Rd., #13, Chandler, AZ 85248 ²
No. 21 - Current Partners, Officers, Directors and Shareholders	Arizona Village Communities Operating Company, 1777 W. Ocotillo Rd., #13, Chandler, AZ 85248

¹ Desert Fox Associates was the previous name of one of the moving entities in this motion, AVC Service Company, LLC.

² AVC is also one of the moving parties in the instant motion.

DN 25 - Equity Security Holders

Arizona Village Communities Operating Company ("AVC") - 100%

Estrella 08-6836

DN 16 - Schedules

Schedule H - Leases	<ul style="list-style-type: none">• Arizona Village Communities Operating Company• Richard and Susan Harkins• Richard and Rea Heesch• Villas at Ocotillo, LLC (of which Arizona Village Communities Operating Company and Heesch Family Revocable Living Trust are equity members)
---------------------	---

DN 17 - Statement of Financial Affairs

No 3 - Payments to Creditors Within One Year	<ul style="list-style-type: none">• Arizona Village Communities Operating Company• Desert Fox Associates
No 19 - Location of Books and Records	Arizona Village Communities Operating Company
No 21 - Current Partners, Officers, Directors and Shareholders	Arizona Village Communities Operating Company - 100%

DN 18 - Equity Holders

Arizona Village Communities Operating Company - 100%

TVAO Case 08-6837

DN 21 - Schedules

Schedule F - Unsecured Creditors	<ul style="list-style-type: none">• Desert Fox Associates 1777 W. Ocotillo, #15 Chandler, AZ 85248 \$193,484.29• Richard H. Heesch \$481.27
----------------------------------	--

Schedule G - Leases	<ul style="list-style-type: none"> • Susan Harkins • Richard Heesch
Schedule H - Co-Debtors	<ul style="list-style-type: none"> • Arizona Village Communities Operating Company 1777 W. Ocotillo, #15 Chandler, AZ 85248 • Richard and Susan Harkins • Richard and Rea Heesch

DN 22 - Statement of Financial Affairs

No 3 - Payments to Creditors Within One Year	<ul style="list-style-type: none"> • Desert Fox Associates (affiliate) • Susan Harkins (insider) • Richard Heesch (insider)
No 21 - Current Partners, Officers, Directors and Shareholders	<ul style="list-style-type: none"> • Arizona Village Communities Operating Company • Heesch Family Revocable Living Trust

DN 23 - Equity Security Holders

Arizona Village Communities Operating Company - 100% (of Class C Equity Holders)

C. The State Court Litigation

While these three bankruptcy cases were proceeding, Debtor TVAO, together with the two moving parties herein, AVC and Desert Fox, filed a state court action against KCB. That action was filed on February 17, 2009, and was signed by attorney Gregory E. Williams of the Phoenix law firm of Koeller, Nebecker, Carlson & Haluck, LLP ("KNCH"). While the Debtor TVAO did not need court authority to file the lawsuit (FED. R. BANKR. P. 6009), its attorneys, as special counsel, did need permission to act for TVAO. That permission was never granted by the bankruptcy court. That permission had been sought by KNCH on January 23, 2009 (DN 90, 08-6834). After consideration of the application, it was denied on March 5, 2009 (DN 111, 08-6834). Importantly, however, is at least one statement made in the KNCH application:

1 The Debtors are related entities owned directly or indirectly by The Arizona
2 Villages Communities Operating Company (the "AVC OpCo"), which also
3 controls other entities related to the Debtors. One such entity is AVC Service
4 Company, L.L.C.³ ("AVC ServCo"), which was formed to manage the Debtors
5 and its affiliates.

6 (DN 90, No.08-6834, at 2-3, lines 25-26; 1-2.) The pleading also noted that "all the claims arise
7 from the same transaction." (DN 90, 08-6834, at 3, l. 10.)

8 The proposed litigation costs were to be paid by, and any recovery shared with, two
9 individuals, George T. Simmons, III and Robert Turpin, "who were directors of AVC and [who]
10 remain existing investors of, and in, AVC and its affiliate companies." (DN 90, Ex. 3, emphasis
11 supplied.)

12 Simultaneously with the application to employ KNCB as special counsel, Debtor
13 TVAO sought approval, by motion, to commence litigation against KCB (DN 91, 08-6834). That
14 motion was denied on March 5, 2009 (DN 111, 08-6834). In spite of these judicial decisions,
15 KNCH, nonetheless, went forward and filed the state court action against KCB on February 17,
16 2009. (See Ex. D to KCB response DN 54, 08-6837.)

17 **D. The Inter-Relationships**

18 Thus, as can be seen from the foregoing analysis, and as additionally set forth in more
19 detail in the entire record of the three cases and as further argued in the KCB response to the instant
20 motion, the connection between the three Debtors and the two moving entities (AVC and Desert
21 Fox⁴), Richard C. Harkins and Richard Heesch are express, evident and clearly identified.

22 Thus, in view of this background, the legal issue becomes--are AVC and Desert Fox
23 bound by the plan?
24
25
26

27 ³ AVC ServCo was formerly Desert Fox Associates.

28 ⁴ Desert Fox changed its name to AVC Service Co., LLC. ("AVC ServCo"). AVC
ServCo and AVC are the moving parties hereunder.

- 1
- 2
- 3
- 4
- 5
- 6
- 7
- 8
- 9
- 10
- 11
- 12
- 13
- 14
- 15
- 16
- 17
- 18
- 19
- 20
- 21
- 22
- 23
- 24
- 25
- 26
- 27
- 28

The amended KCB plan was noticed out to, among others:

Ms. AZ Designs
c/o Susan Harkins
9665 E. Caron Street
Scottsdale, AZ 85258-5600

9

1 The principal components of the KCB plan provided for a cash infusion, upon the
2 plan's effective date, of \$110,000, and a waiver of KCB's unsecured claim against the estate of
3 \$681,038.

4 In the definitions section of the KCB amended plan, the two moving parties here were
5 expressly defined as:

6 2.5. **AVC Parent Company** shall mean AVC Operating Company Inc.

7 2.6. **AVC Service Company** shall mean AVC Service Company, L.L.C.⁵

8
9 (Plan, at 2.) In addition, the plan also expressly defined the state court litigation pending against
10 KCB (Maricopa County Superior Court Case CV2009-002600) as:

11 2.37 **KCB Litigation** shall mean any and all claims or causes of
12 action asserted in the case now pending in The Villas at Ocotillo, LLC
13 et al. v. Kitchell Custom Builders, LLC, et al., Superior Court of the
14 State of Arizona, Maricopa County, No. CV2009-002600, including
any amendments or additions to such claims or causes of action.

15 (Plan, at 6, emphasis supplied.) Further, the definition section of the amended plan also referred to
16 the "KCB Plaintiffs" as:

17 2.39. **KCB Plaintiffs** shall mean TVAO, the AVC Parent Company, and the
18 AVC Service Company, any purported assignees of the claims or causes of
19 action asserted by TVAO, the AVC Parent Company, and the AVC Service
20 Company in the KCB Litigation, any purported successors to TVAO, the AVC
21 Parent Company, and/or the AVC Service Company, and any person claiming
by or through TVAO, the AVC Parent Company, and/or the AVC Service
Company that seeks to assert a claim against KCB of the same type as the
claims at issue in the KCB Litigation.

22 (Plan at 6, emphasis added.) In the section describing how the plan was to be implemented, KCB's
23 plan provided:

24 6.1. **KCB Contribution.** Within five (5) business days of the Effective
25 Date, KCB shall pay to the Disbursing Agent the sum of \$110,000.00 for
26 distribution to the holders of Allowed Claims under this Plan.

27
28

⁵ Formerly, Desert Fox Associates.

1 In exchange for the KCB Contribution, the claims asserted by the KCB
2 Plaintiffs in the KCB Litigation shall be dismissed with prejudice, and the
3 KCB Plaintiffs shall be deemed to have released [and] forever discharged
4 KCB, KCB Custom Homes, Inc., KCB Corporation, Inc. (the "Released
5 Parties"), from and against any and all claims, obligations, demands, liabilities,
6 actions, causes of action, debts, contracts, controversies, agreements, promises,
7 damages, demands and liabilities whatsoever, which the KCB Plaintiffs may
8 ever have had, now has, or hereafter may have (whether known or unknown),
9 relating to or arising in any manner from or as a result of the actions or events
10 at issue in the KCB Litigation; provided, however, that such release shall not
11 affect any obligation of KCB under this Plan. The Released Parties shall
12 include all of their successors, assigns, parents, subsidiaries, affiliates,
13 employees, agents, owners, operators, managers, officers, directors, attorneys,
14 shareholders, and professionals.

6.2. **Waiver of KCB Claim.** In addition to making the KCB Contribution,
KCB shall waive and forego its right to any distribution under this Plan on
account of the KCB Claim and the KCB Mechanic's Liens. Nonetheless, KCB
shall be entitled to vote the KCB Claim and the KCB Contribution.

(Plan at 11.) This important aspect of the plan was spelled out again in the plan:

6.14. **Settlement and Release of Causes of Action.** The KCB Litigation
shall be settled and all claims and causes of action asserted by the KCB
Plaintiffs shall be released in accordance with the provisions of §6.1 of the
Plan. Any other Causes of Action that the Debtors may be entitled to assert
shall be abandoned, released, and/or waived.

(Plan at 13, emphasis supplied.) And, to emphasize that this estate had very few, if any other assets,
the KCB plan noted:

6.10 **Funding of the Plan.** The Plan shall be funded entirely by the KCB
Contribution and the proceeds, if any, resulting from the sale of the personal
property in TVAO Unit 16 pursuant to the Sale Motion.

(Plan at 12.)

The motivation for the KCB plan, its monetary contribution, its waiver of claim and
its release from further litigation with the "KBC Plaintiffs" (Debtor TVAO, Desert Fox and AVC),
was simply to disentangle itself, once and for all, from its connection to the three Debtors, the
Debtors' affiliates and those individuals who controlled them. This type of plan is not unique to
bankruptcy practice, and the Code envisions and encourages creative provisions which are designed
to cut all sorts of legal Gordian knots. *See, e.g., 11 U.S.C. § 1123(b)(1) and (6); see also In re*

1 *Associated Vintage Group, Inc.*, 283 B.R. 549, 560 (9th Cir. BAP 2002) (“[t]he hallmark of chapter
2 11 is flexibility in which the content of plans is primarily up to the genius of the drafter.”)

3 4 **F. The Voting**

5
6 The KCB plan was noticed out for the creditors to vote on. Among those casting votes
7 against the plan were AVC (two votes) and Desert Fox Associates (one vote). Both the AVC and
8 Desert Fox ballots were signed by Richard C. Harkins, as either president (AVC) or manager (Desert
9 Fox). In each ballot, AVC and Desert Fox self-identified themselves as holding Class 4 general
10 unsecured claims against TVAO. (*See* Ex. F to KCB response.)

11 With those ballots, both AVC and Desert Fox thrust themselves directly and squarely
12 into participation in the TVAO case, in addition to all of the other cross-connections and close inter-
13 relationships noted throughout the entire record in these cases. If there had been any doubt as to
14 their involvement before they voted, none existed once those ballots were cast.

15 16 **G. The Confirmation Hearing**

17
18 In its order setting the hearing on confirmation for July 28, 2009, the court's order,
19 which accompanied the KCB plan, disclosure statement and ballot, stated that any objections to the
20 KCB plan must be in writing and filed within five days prior to the hearing (DN 179, 08-6834).
21 Neither AVC nor Desert Fox filed a written objection to the KCB plan, nor offered a spoken
22 objection at the hearing. This decision to do nothing was highlighted by the appearance of their
23 same KNCH state court counsel, who appeared but only on behalf of another, unrelated creditor.

24 Thus, after notice and without any legal objection having been made by either AVC
25 or Desert Fox, the court confirmed the KCB plan (DN 201, 08-6834). The confirmation order was
26 entered on August 13, 2009 (DN 201, 08-6834).

- 1
- 2
- 3
- 4
- 5
- 6
- 7
- 8
- 9
- 0
- 1
- 2
- 3
- 4
- 5
- 6
- 7
- 8
- 9
- 0
- 1
- 2
- 3
- 4
- 5
- 6
- 7
- 8

3
4

5
6
7
8

9

1

3
4

5
6
7
8
9
20
21

22
23
2426
27

1 12.8 Resolve any cases, controversies, suits, or disputes that may arise in
2 connection with the consummation, interpretation, or enforcement of this Plan,
or any person's obligations incurred in connection with this Plan; . . .

3 * * *

4 12.10 Issue injunctions, enter and implement other orders, or take any other
5 necessary or appropriate actions to restrain any entity's interference with
consummation or enforcement of this Plan;

6 (Plan at 19-20, emphasis supplied.)
7
8
9

10 **ISSUES PRESENTED**

- 11 1. Is AVC Service Company, LLC ("Desert Fox Associates") bound by
12 the plan?
13
14 2. Is The Arizona Village Communities Operating Company, Inc.
15 ("AVC") bound by the plan?

16 **LEGAL DISCUSSION**

17
18 Each of the issues involve questions of fundamental procedural due process, as well
19 as whether substantive obligations were created by the plan. As for procedure, the court must decide
20 if each of the moving parties had sufficient notice of the proceedings, which required them to voice
21 objections. If so, are they now included in the plan's provisions, and can they be held to have
22 substantively waived the right to object to the dismissal, with prejudice, of the KCB litigation
23 pending in state court? The Bankruptcy Code clearly sets forth the effect of a confirmation order:
24

25 " . . . the provisions of a 'confirmed plan' bind the debtor . . . and any creditor,
26 equity security holder, or general partner in the debtor . . . "

27 11 U.S.C. § 1141(a). This statute is clear and unambiguous.
28

1 In addition to the statute, the Ninth Circuit has, on more than one occasion, held that
2 an interested party is bound by the plan, even if the plan contained language which might not have
3 passed a legal challenge. In other words, if a party has sufficient notice, but elects not to voice an
4 objection, and a plan which is detrimental to that party's rights is confirmed, that party will be
5 legally bound by the plan. *In re Heritage Hotel P'ship I*, 160 B.R.374 (9th Cir. BAP 1993), *aff'd*,
6 59 F.3d 175 (9th Cir. 1995) (unpub. mem. dec.); *In re Pardee*, 193 F.3d 1083, 1086 (9th Cir. 1999)
7 (citing *Trulis v. Barton*, 107 F.3d 685, 691 (9th Cir. 1995)); *Espinosa v. United Student Aid Funds,*
8 *Inc.*, 553 F.3d 1193 (9th Cir. 2008). Even faulty orders are entitled, at some point, to finality.
9 *Pardee*, 193 F.3d at 1086; *Espinosa*, 553 F.3d at 1199.

10 As can be seen from the recitation herein, both AVC, Desert Fox and the individuals
11 controlling them were deeply involved in these cases. They have involvement in every way and at
12 every level--financial, contractual, managerial, ownership, and creditors. It is too late to now claim
13 that they should be free to carry on litigation against the KCB entities. They were given clear notice
14 of a plan which was going to affect their legal rights. They chose to do nothing.

15 On the other hand, KCB diligently and methodologically exercised its legal rights, and
16 did so openly. The plan was clear as to what it intended to do, and how it proposed to do it.
17 Creditors voted for the plan in the appropriate percentages, and the plan was confirmed. KCB has
18 agreed to pay \$110,000 in cash, and to release its claim of \$681,038, in exchange for a release of
19 litigation, which, by AVC and Desert Fox's own attorneys' statement, arises out of the same claim
20 as that held by the Debtor TVAO.

21 The involvement of AVC, Desert Fox and its principals rise far above the "mere
22 overlap" stated in their motion. They have been in too deep, for too long, to now claim innocent
23 third-party status.

24 AVC and Desert Fox are bound by the plan, and they must dismiss the KCB litigation
25 with prejudice, once KCB fulfills its commitment to fund the plan and waive its claim.

26 Finally, on a procedural note, the Rule 59 motion to alter or amend fails as well. This
27 is because the court has not been given a chance to change anything. The arguments made are
28 objections that should have been made in the first instance. The court has not been told why it

1 should re-think what it did, due to either misperceived facts or misapplied law, by parties who failed
2 to initially object on a timely basis or who disagree with the court's decision. *See, e.g., Above the*
3 *Belt, Inc. v. Mel Bohannon Roofing, Inc.*, 99 F.R.D. 99, 101 (E.D. Va. 1983).

4 The time for AVC and Desert Fox to have made these arguments was as an objection
5 to the plan, not raise them for the first time once a plan has been noticed, voted upon, a hearing held,
6 and a confirmation order entered.

7
8 **RULING**

9
10 Therefore, the FED. R. CIV. P. 59 motion, filed by AVC and Desert Fox, to alter or
11 amend the confirmation order will be DENIED. A separate order will be entered. Bank. R. 9021.

12
13 DATED AND SIGNED ABOVE.

14
15 COPIES to be sent by the Bankruptcy Notification
16 Center ("BNC") to the following:

17 William A. Nebeker
18 Koeller Nebeker Carlson & Haluck
3200 N. Central Ave., #2300
Phoenix, AZ 85012

Email: nebeker@knchlaw.com

19 Scott B. Cohen
20 Engelman Berger
3636 N. Central Avenue, Suite 700
Phoenix, AZ 85012

Email: sbc@engelmanberger.com

21 Dale C. Schian
22 Schian Walker
3550 N. Central Ave. #1700
23 Phoenix, AZ 85012-2115

Email: ecfdocket@swazlaw.com

24 James W. Armstrong
25 Sacks Tierney, P.A.
4250 North Drinkwater Boulevard, 4thFloor
Scottsdale, AZ 85251-3693

Email: james.armstrong@sackstierney.com

26 Larry Lee Watson
27 Office of the U.S. Trustee
230 North First Avenue, Suite 204
28 Phoenix, AZ 85003-1706

Email: larry.watson@usdoj.gov